

Release Number: 201517026

INTERNAL REVENUE SERVICE

Release Date: 4/24/2015

TE/GE TECHNICAL ADVICE MEMORANDUM

Date: January 29, 2015

Uniform Issue List: 7805.00-00

Internal Revenue Service

Attn:

Program Manager

Office of Appeals, Domestic Operations

Taxpayer's Name:

Taxpayer's Address:

Taxpayer's Identification Number:

Year Involved:

Legend:

<u>Corporation</u>	=
<u>Program</u>	=
<u>Program Application</u>	=
<u>Date 1</u>	=
<u>Date 2</u>	=
<u>Date 3</u>	=

**ISSUE:**

Whether the Commissioner, TE/GE should exercise discretion to grant Corporation relief under I.R.C. § 7805(b) to limit the retroactive effect of revocation of its exempt status under § 501(c)(3).

**Facts as Presented on Form 1023:**

Corporation was incorporated on Date 1 and was recognized exempt from federal taxation under § 501(c)(3) and classified as a public charity under §§ 170(b)(1)(A)(vi) and 509(a)(1) in a determination letter dated Date 2. The determination was based solely on the representations made in the Application for Exemption and the supplemental statements attached to the application.

Corporation stated that it would be providing Program gifts to individuals and families for the purpose of purchasing a home. In addition, Corporation stated "to qualify, people must fall into

either low or moderate-income categories as defined by FHA and/or Fannie Mae. They must qualify for a mortgage, demonstrate a need for Program assistance and purchase a home in the program. We will promote our program through real estate agents, mortgage lenders and homesellers/builders”.

During the Appeals Process, Corporation submitted a Request for Relief under Section 7805(b). Corporation states in its Request for Relief that they submitted a brochure with its original Application for Exemption (Corporation also submitted a copy of an Application for Exemption that it claims that it filed with the Service as a supporting document in their Request for Relief); the brochure contained a statement that Corporation would operate with no geographic limitations and no income limitations. Corporation argues that this brochure put the Service on notice and that the Service should have been aware of the manner that Corporation was promoting the Program upon careful review of the materials.

In addition, Corporation also submitted a copy of their Program Guidelines that it claimed was also submitted with its Application for Exemption. However, a review of the official record of the Application for Exemption received from EO Determinations revealed that the brochure was in fact not included with Corporation's filed Application for Exemption.

In addition, a review of the Program Guidelines that was submitted with their original Application for Exemption revealed that there are several discrepancies between the document submitted with their original Application for Exemption and Request for Relief.

**Facts as Developed During the Examination Process and Appeals Process:**

During the period under examination, Corporation's primary activity was the operation of a nationwide Program under which Corporation was merely acting as a broker to facilitate the selling of homes. Corporation operated without income limitations and did not screen homebuyers for Program funds based on income or geographical limitations. Since its inception, Corporation has promoted and operated a Program for homebuyers under which they provide funds to the homebuyer to use as their down payment and collects the same amount, plus an additional fee from the homeseller. Corporation derived 99% of its revenue from the service fee charged to homesellers. Corporation did not solicit funds from the general public or government. Corporation was funded entirely from the service fee that was charged to the homeseller for enrolling their home in the Corporation Program.

Corporation restricted the use of the gift to the purchase of a home that was enrolled in the Corporation Program. Corporation required homesellers or builders to enter into an agreement to pay a service fee. The service fee was comprised of a program fee and a processing fee. The program fee was always equal to the amount of Program funds that Corporation provided to the homebuyer.

Corporation did not have any income limitations for its Program and did not screen homebuyers to determine if they qualified as low to moderate income homebuyers or limit its Program to low or moderate income homebuyers. Corporation's promotional materials state that Program funds are available to anyone who qualifies for a mortgage. Corporation represented that 57 percent of homebuyers that they assisted were in the middle-income census track. Corporation made this finding only after it provided Program assistance to the homebuyers. In addition, Corporation's promotional material and advertising make it clear that its Program was open to anyone who, without any income limitations, otherwise qualified for a home mortgage.

The examination documented that Corporation's Application for Program does not contain any questions to establish whether the applicant is in the low to moderate income level. A document that is completed by the lender does request the homebuyer's income. However, these documents are sent to Corporation only after the homebuyer has been approved for a mortgage.

Corporation asserted during the examination that its Program is designed to assist a charitable class because only a house of a specified value may be enrolled in the program. However, the examination discovered no evidence that Corporation limited the enrollment of homes to the specified limit.

Corporation did not limit its assistance to homes located in geographical areas experiencing economic depression or deterioration. Rather, Corporation made Program funds available for any property, provided that the homeseller or home builder agree to remit to Corporation the amount correlating to the amount of Program funds transferred to the homebuyer, pay the service fee, and the buyer qualifies for a mortgage, usually a FHA insured mortgage.

Corporation recommended that potential homebuyers take a free online homeownership course, but did not require that the homebuyer complete the course to receive funds from the Program. In addition, Corporation did not conduct educational activities.

The examination concluded that during the years under examination, Corporation did not qualify for tax-exempt status under § 501(c)(3). The examination recommended that Corporation's exemption letter be revoked effective as of the first day of the examination period for the following reasons:

- Corporation's Program was operated in a manner similar to the organization described Rev. Rul. 2006-27, 2006-1 C.B. 915 (May 22, 2006),
- Corporation operated primarily for the benefit of homesellers,
- Corporation failed to establish that its activities lessen the burdens of government, and Taxpayer appealed the proposed revocation. The Office of Appeals sustained the revocation. Section 4.04 of Rev. Proc. 2014-5, 2014-1 I.R.B. 169, 173 states that all requests for § 7805(b)

relief are mandatory TAM's with respect to all exempt organizations. Delegation Order 30-1 (formerly DO-96, Rev. 13) delegates authority to the Commissioner, Tax Exempt and Government Entities (TEGE), to prescribe the extent to which any ruling relating to the internal revenue laws shall be applied without retroactive effect.

Corporation requests that the Commissioner TEGE exercise discretion and grant relief to limit the retroactive effect of revocation under § 7805(b) to Date3.

**Law:**

I.R.C. 7805(b)(8) provides that the Secretary may prescribe the extent, if any, to which any ruling (including any judicial decision or any administrative determination other than by regulation) relating to the internal revenue laws shall be applied without retroactive effect.

Treas. Reg. § 1.501(a)-1(a)(2) state that an organization that has been determined by the Commissioner to be exempt under § 501(a) may rely upon such determination so long as there are no substantial changes in the organization's character, purposes, or methods of operation, and subject to the Commissioner's inherent power to revoke rulings because of a change in the law or regulations, or for other good cause.

Treas. Reg. § 301.7805(b)-1 grants to the Commissioner authority to prescribe the extent to which any ruling issued by his authorization shall be applied without retroactive effect.

Treas. Reg. § 601.201(l)(1) states that a ruling (or a determination letter per § 601.201(m) may be revoked or modified at any time in the wise administration of the taxing statutes.

Treas. Reg. § 601.201(l)(4) states that a ruling found to be in error or not in accord with the current views of the Service may be modified or revoked by notice to the taxpayer.

Treas. Reg. § 601.201(n)(3)(ii) states that a ruling or determination letter recognizing exemption may not be relied on if there is a material change inconsistent with the exemption in the character, the purpose, or the method of operation of the organization.

Treas. Reg. § 601.201(n)(6)(i) addressing the revocation or modification of determination letters on exemption and foundation status, provides that such revocation may be retroactive if the organization omitted or misstated a material fact or operated in a manner materially different from that originally represented. Revocation or modification will ordinarily take effect no later than the time at which the organization received written notice that its exemption ruling or determination letter might be revoked or modified.

Rev. Proc. 2014-5, 2014-1 I.R.B. 169, § 4.04 states that all requests for relief under § 7805(b) must be made through a request for technical advice (TAM). Section 19.04 states further that

when, during the course of an examination by EO Examinations or consideration by the Appeals Area Director, a taxpayer is informed of a proposed revocation, a request to limit the retroactive application of the revocation must itself be made in the form of a request for a TAM and should discuss the items listed in section 18.06 as they relate to the taxpayer's situation.

Section 18 of Rev. Proc. 2014-5, lists the criteria necessary for granting section 7805(b) relief as well as the effect of such relief. Section 18.06 states, in part, that a TAM that revokes a determination letter is not applied retroactively if:

- (1) there has been no misstatement or omission of material facts;
- (2) the facts at the time of the transaction are not materially different from the facts on which the determination letter was based;
- (3) there has been no change in the applicable law; and
- (4) the taxpayer directly involved in the determination letter acted in good faith in relying on the determination letter, and the retroactive revocation would be to the taxpayer's detriment.

Rev. Proc. 2014-9, 2014-2 I.R.B. 281, sets forth procedures for issuing determination letters (from EO Determinations) and rulings (on applications for recognition of exempt status by EO Technical) on the exempt status of organizations under § 501. These procedures also apply to revocation or modification of determination letters or rulings.

Section 12.01 of Rev. Proc. 2014-9, states, in part, that the revocation or modification of a determination letter or ruling recognizing exemption may be retroactive if the organization omitted or misstated a material fact, or operated in a manner materially different from that originally represented. In certain cases an organization may seek relief from retroactive revocation or modification of a determination or ruling under § 7805(b) using the procedures set forth in Rev. Proc. 2014-4, which further refers to Rev. Proc. 2014-5, sections 18 and 19.

Section 12.01(1) of Rev. Proc. 2014-9, states that where there is a material change inconsistent with exemption in the character, the purpose, or the method of operation of an organization, revocation or modification will ordinarily take effect as of the date of such material change.

**Taxpayer's Position:**

In their request for relief under § 7805(b), Corporation represented that under § 601.201(l)(5) relief should be granted because:

- (1) Corporation made no misstatement or omission of material facts;
- (2) Corporation operated in a manner not materially different from the facts stated in its Application for Exemption, on which the exemption was granted on Date 2.

- (3) There has been no change in the applicable law;
- (4) The organization acted in good faith in relying on the Date2 determination letter and retroactive revocation would be to their detriment.

Corporation represents that it submitted a copy of a brochure with its Application for Exemption describing how it planned to distribute and promote their Program. In this brochure, it states that Corporation would operate their Program with no income restrictions or geographic limitations. As such the Service should have been aware of this manner of promoting the Program and should not be allowed to rely on the no income limitations statement to retroactively revoke its exempt status.

**Government's Position:**

A taxpayer may rely on a ruling or determination letter, assuming that the taxpayer does not make any material changes inconsistent with its exemption in its character, purpose or method of operation. §§ 601.201(n)(3)(ii) and 1.501(a)-1(a)(2). If the taxpayer does make such material changes, revocation of exempt status will ordinarily take effect as of the date of the change. Section 12.01(1), Rev. Proc. 2014-9. However, revocation may be retroactive if the taxpayer omitted or misstated material facts. § 601.201(n)(6)(i). Even if the taxpayer has not changed or misstated any facts, the Commissioner may correct an error in a prior ruling. § 601.201(l)(4).

The procedures for requesting retroactive relief are described in § 18 of Rev. Proc. 2014-5, supra based on § 601.201(l)(5). A taxpayer may be eligible for relief if it has made no misstatements or omissions of material facts; if the facts at the time of the transaction are not materially different from the facts on which the determination was based; there has been no change in the law; and the taxpayer relied in good faith on the determination letter. Relief is not always available, even under these circumstances. The Commissioner may correct a mistake by the Service, even if the taxpayer has not changed its behavior and had relied on the earlier ruling.

Revocation of an organization's determination letter recognizing exempt status may be retroactive if the organization omitted or misstated a material fact. § 601.201(n)(6)(i). Corporation did omit or misstate a material fact and operated in a manner materially different from that was originally represented in its Application for Exemption.

Corporation has omitted material facts and has operated in a manner materially different from the facts as represented in its Application for Exemption. Therefore, it is appropriate to revoke Corporation' determination letter recognizing it as a tax-exempt organization retroactively to Date 3, the date it was determined that Corporation operated in a way that was materially different than that described in its Application for Exemption.

Instead of operating in the manner as described in its Application for Exemption on which its determination was made, Corporation began operating a seller-financed Program without any income or geographical limitations on a nationwide basis. In addition, Corporation did not screen its Program recipients on the basis of income. Corporation provided funds to any homebuyer who qualified for a home mortgage.

Corporation claims that they submitted a copy of a brochure that states that they would operate their program without geographical limitations and no income limitations with their Application for Exemption. However, a review of the official administrative record received from EO Determinations revealed that this brochure was in fact not submitted with their Application for Exemption. In addition, Corporation submitted a copy of their Program Guidelines with their Request for Relief that contained several discrepancies when compared to the document submitted with their Application for Exemption. Therefore, Corporation misstated and omitted material facts and operated in a manner materially different from that originally represented in its application.

Corporation has not satisfied all of the requirements under § 18.06 of Rev. Proc. 2014-5 for granting such relief for the following reasons:

- (1) Corporation omitted material facts in its Application for Exemption.
- (2) Corporation operated in a manner materially different from the facts under which the determination letter granting exemption was issued.
- (3) There has been no change in the applicable law.
- (4) Corporation did not act in good faith in relying on the determination letter and retroactive revocation would be to their detriment.

Corporation has omitted material facts and has operated in a manner materially different from the facts as represented in its Application for Exemption therefore, it is appropriate to revoke Corporation' determination letter recognizing it as a tax-exempt organization back to the effective date of the determination letter.

**Recommendation:**

The Commissioner, TE/GE, exercises discretion to deny Corporation relief under I.R.C. 7805(b) because Corporation has made material misstatements and its operations are materially different from what was represented in its Application for Exemption. Therefore, it is appropriate to revoke Corporation's determination letter dated Date 2 effective as of the first day of the examination period which is Date 3.

This ruling is based on the facts as they were presented and on the understanding that there will

be no material changes in these facts. This ruling does not address the applicability of any section of the Code or regulations to the facts submitted other than with respect to the sections described. Because it could help resolved questions concerning your federal income tax status, this ruling should be kept in your permanent records.

A copy of this memorandum is to be given to Corporation. Section 6110(k)(3) provides that it may not be used or cited as precedent.

-END-